MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 1, 2022/2023 (TERM ID 2210)

BAC3624 – ADVANCED AUDITING

(All sections/Groups)

13 FEBRUARY 2023
9.00 a.m – 12.00 p.m
(3 Hours)

INSTRUCTIONS TO STUDENT

1. This question paper consists of 9 pages excluding cover page with 5 Questions only.
2. Answer all **FIVE** questions. Mark distribution for each question is given.
3. Please write all your answers in the Answer Booklet provided.
4. All questions must be answered in English.

QUESTION 1

a) Your firm is the external auditor of Biru Berhad (Biru). The directors of Biru discovered a fraud soon after the auditor's report on the financial statements for the year ended 30 June 2022 was signed. Some of Biru's employees had given unauthorised discounts on sales made to their friends and families, which is not allowed by Biru's discount policy. The amounts were not material to the financial statements, but Biru's managing director has expressed concern that your firm did not discover this fraud during the audit. Outline the responsibilities of your firm and Biru's directors in respect of this fraud and reach a conclusion as to whether those responsibilities were met. (4 marks)

b) Your firm has identified that the total fees from the provision of audit and non-audit services to Merah Berhad (Merah), a listed company, is expected to amount to 6% of your firm's annual fee income in 2022. State, with reasons, the steps that the engagement partner of Merah should take, including any safeguards that might be necessary. (3 marks)

c) Kuning Berhad (Kuning) is an international engineering company. Your firm has accepted an engagement to provide a limited assurance report on safety performance indicators included in Kuning's published corporate responsibility report. One such safety performance indicator is the number of workplace accidents by employees, per million working hours, at each of its international engineering plants. List three assurance procedures that your firm could perform in relation to the number of workplace accidents performance indicator. (3 marks)

d) You are working on the external audit of Hijau Berhad (Hijau) for the year ended 31 August 2022. You are responsible for performing the planned procedures in respect of trade receivables. Your analytical procedures identified that receivables days have increased from 35 days at 31 August 2021 to 43 days at 31 August 2022. On enquiry, Hijau's financial controller explained: "The increase is due to a contract for the supply of goods to a new customer, Putih Berhad (Putih). The contract allows Putih 60 days' credit rather than our standard 30 days' credit. We despatched a large order to Putih 50 days before the year end." Outline the additional audit procedures you would perform in respect of the financial controller's explanation. (4 marks)

e) During your firm's external audit of the financial statements of Brown Berhad, the audit team has identified a number of misstatements. No individual misstatement is material. Outline the actions that should be taken in respect of these misstatements before the auditor's report is signed. (3 marks)

Continued ...

f) The financial statements of Pink Berhad (Pink) include an investment in Hitam Berhad (Hitam) stated at RM7.8 million. The external auditor has concluded that the investment in Hitam should be recognised at RM2 million. The directors of Pink have refused to recognise the reduction in the value of the investment. The profit before tax of Pink is RM46.7 million and gross assets are RM824 million.

State, with reasons, the implications for the auditor's report.

(3 marks)

(Total: 20 marks)

QUESTION 2

Your firm is the external auditor of Tele Berhad (Tele) and you are the senior responsible for planning the audit for the year ended 31 August 2022. Your firm performed an engagement to review Tele's financial statements for the year ended 31 August 2021 but Tele is now required to have an external audit of its financial statements for the first time.

Tele installs and operates charging points which are used to recharge the batteries in electric vehicles. Tele earns revenue from (a) the sale and installation of charging points at customers' homes and (b) income from electric vehicle owners who use Tele's network of charging points located in public car parks.

Tele has experienced rapid growth due to an increase in electric vehicle ownership. The Malaysia Society of Motor Manufacturers, which publishes industry data, reported that ownership of electric vehicles grew by 52% between August 2021 and August 2022. The engagement partner has asked you to consider the following key areas of audit risk:

(1) Revenue
(2) Rental expenses relating to charging points in public car parks
(3) Property, plant and equipment – charging points in public car parks.

The sales price of charging points, including installation at customers' homes, is RM800. Customers can claim RM500 contribution towards this cost from the Malaysian government's Office for Low Emission Vehicles (OLEV). Tele manages the process to claim the contribution by providing claim forms to the customer for completion. The contribution is subject to the customer complying with a list of conditions specified on the claim form.

Tele sends completed customer claim forms to OLEV and receives RM500 directly from OLEV providing the claim form demonstrates compliance with the list of conditions. Customers pay Tele the net amount of RM300, online, prior to the installation. Tele recognises RM800 as revenue on the day of installation. It also records a receivable of RM500 as Tele does not receive the contribution from OLEV until several weeks after the installation has taken place.

Continued ...

Your firm visited Tele in July 2022 and identified two internal control deficiencies relating to claims for the RM500 contribution from OLEV. Prior to sending customer claim forms to OLEV:

- the sequential numbering of the forms was not checked for gaps in the sequence
- not all claims were checked for compliance with the conditions required by OLEV

Tele also owns charging points located in public car parks such as those at supermarkets. Owners of electric vehicles pay Tele for each minute of charging. To use these charging points, owners of electric vehicles must register an account on Tele's website and provide personal data including a credit card number. On registration, owners are sent a Tele card which they insert into the charging point to recharge their car batteries. Owners add funds to their online accounts using a credit card. Usage data from each charging point is transmitted to Tele's business information system and the amount due is deducted from the vehicle owner's account. Data from the business information system is used to update Tele's nominal ledger accounts.

Tele pays a fixed rent, quarterly in arrears, to the owners of the public car parks in which its charging points are located. Each rental agreement specifies a maximum number of total minutes of charging. If the maximum number of minutes is exceeded, then additional rent becomes payable to the car park owner. Any additional rent is payable each year on the anniversary of the rental agreement. Tele accrues for the additional rent relating to agreements that straddle the year end. The accrual is calculated by multiplying the rate specified in the agreement with the estimated number of additional minutes used, for the months between the anniversary of the agreement and 31 August.

Charging points are assembled in Tele's Malaysia factory using components that are sourced from around the world. Suppliers invoice Tele in their local currency.

Charging points located in public car parks are capitalised as property, plant and equipment and depreciated at 25% per year using the reducing balance method. The total costs capitalised include the cost of the components, labour costs and overheads. The capitalised overhead cost is estimated by Tele's finance director, Rahman, and is based on a proportion of the total overhead costs recorded in the management accounts.

During 2022, Tele developed an app for smartphones which allows electric vehicle owners to register an account and use charging stations without a Tele card. This development required Tele to modify each of its charging points so they can be operated with the new app. The costs of the modifications have been capitalised and included in charging points in property, plant and equipment.

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During your planning meeting, Rahman provided the following information:

Statement of profit or loss for the year ended 31 August (extract)

	2022 (draft) RM'000	2021 (reviewed) RM'000
Revenue		
Home charging point installations (Note 1)	10,205	4,277
Public car park charging point usage	8,976	3,122
	19,181	7,399
Cost of sales (Note 2)	(16,022)	(6,516)
Gross profit	3,159	883

Note: to the financial statements for the year ended 31 August (extract) Property, plant and equipment – public charging points.

	2022 (draft) RM'000	2021 (reviewed) RM'000
Carrying amount at 1 September	5,367	4,876
Additions	4,777	1,998
Depreciation charge	(1,932)	(1,507)
Carrying amount at 31 August	8,212	5,367

Notes

1. Includes amounts received and receivable from OLEV.

2. Includes rental payments and accrual for the year ended 31 August 2022 of RM4,917,000 (2021: RM2,988,000) and depreciation of public charging points.

Rahman also suggested that your firm considers using the data available in Tele's business information system as part of the audit:

Examples of data available in Tele's business information system

- Date and location of each home charging point installation
- Daily usage minutes for each charging point in a public car park
- Faults recorded by each charging point in a public car park
- Customers' personal data

Continued ...

Required:

a) Describe the differences between the scope of the review of Tele's financial statements for the year ended 31 August 2021 and the scope of the external audit of the financial statements for the year ended 31 August 2022. Give reasons for these differences.
(6 marks)

b) Justify why the items listed by the engagement partner have been identified as key areas of audit risk and, for each item, describe the procedures that should be included in the audit plan to address those risks. You should present your answer using the following subheadings:

(i) Revenue
(ii) Rental expenses relating to charging points in public car parks
(iii) Property, plant and equipment – charging points in public car parks
(25 marks)

c) Identify and explain the audit risks that might arise due to Tele storing the personal data supplied by customers. (5 marks)

(Total: 36 marks)

QUESTION 3

Amir & Co is a firm of Chartered Certified Accountants offering audit and assurance services to a large portfolio of clients. You are a manager in the audit department responsible for the audit of Gift Berhad which has a financial year ended 31 July 2022. The audits of both clients are being completed and you are reviewing issues which have been raised by the audit seniors.

Gift Berhad is a manufacturer of luxury food items including chocolate and other confectionery which are often sold as gift items individually or in hampers containing a selection of expensive items from the range of products. Due to an economic recession, sales of products have fallen sharply this year, and measures have been implemented to support the company's cash flow. You are aware that the company only has RM150,000 in cash at the year end.

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Extracts from the draft financial statements and other relevant information are given below:

	Note	July 2022 (Draft) RM'000	July2021 (Actual) RM'000
Revenue		2,440	3,950
Operating expenses		-2,100	-2,800
Finance charge		-520	-500
(Loss)/profit before tax		-180	650
Total assets		10,400	13,500
Long-term liabilities - bank loan	1	3,500	3,000
Short-term liabilities - trade payables	2	900	650
Disclosed in notes to financial statements:			
Undrawn borrowing facilities	3	500	1,000
Contingent liability	4	120	-

Notes

1. The bank loan was extended in March 2022 by drawing on the borrowing facilities offered by the bank. The loan carries a fixed interest rate and is secured on the company's property including the head office and manufacturing site. The first repayment of loan capital is due on 30 June 2023 when RM350,000 is due to be paid.
2. Gift Berhad renegotiated its terms of trade with its main supplier of cocoa beans, and extended payment terms from 50 days to 80 days in order to improve working capital.
3. The borrowing facilities are due to be reviewed by the bank in April 2023 and contain covenants including that interest cover is maintained at a minimum of 2, and the ratio of bank loan to operating profit does not exceed 4:1.
4. The contingent liability relates to a letter of support which Gift Berhad has provided to its main supplier of cane sugar which is facing difficult trading conditions.

Required:

In respect of the audit of Gift Berhad:

a) Evaluate the matters which may cast significant doubt on the company's ability to continue as a going concern. (8 marks)

b) Design the audit procedures to be performed in relation to the going concern matters identified. (7 marks)

(Total: 15 marks)

Continued ...

QUESTION 4

You are a senior manager at ABC & Co, a firm of Chartered Certified Accountants. You are responsible for reviewing quality control and ethical matters which arise with the firm's portfolio of clients. During recent investigations you identified the following matters:

Lily Trading

Lily Trading currently qualifies as a small company in the jurisdiction in which it operates, with revenue of RM7.5 million (2021-RM5.3 million), and as such is not required by law to have an audit. Until recently, your firm has provided a range of non-audit services to Lily Trading including bookkeeping, payroll and tax computation and advice. The company recently obtained an offer for a significant amount of finance to help the company grow. The management of Lily Trading has ambitious plans for growth which they believe will result in revenue doubling within one year and then continuing to grow at a similar annual rate for at least the next five years. In order to secure the funding, the directors have decided to have the financial statements audited and have asked if ABC & Co will become the company's auditors, as well as continuing to provide the existing non-audit services. This will include auditing the financial statements for the year ended 31 July 2022 at the request of the new financers.

Cekap Berhad

You have been approached by Cekap Berhad, a retail company, to provide audit and tax services. In response you have written to the outgoing auditor to ask if there are any matters which you should be made aware of which might prevent you from accepting the assignment. Despite a number of follow up phone calls, you have not been able to obtain a response from the outgoing audit firm. On discussing this with the management team of Cekap Berhad, you are made aware that the company is suing the outgoing auditor for damages due to the detrimental effect on their reputation following the auditor issuing a modified opinion, which the directors of Cekap Berhad felt was inappropriate. The reason for the modified opinion was the application of an accounting treatment which the outgoing auditor considered to be inappropriate and a material misstatement.

Pantas Berhad

Pantas Berhad is a listed audit client of your firm. The management team of Pantas Berhad has asked you to perform a valuation of the shares of another audit client, Syabas Trading, with a view to buying the entire shareholding. Syabas Trading is a private company whose shares are owned entirely by the original founder, Mr Patrick Lim.

Continued ...

Required

Comment on the ethical and other professional issues raised, and recommend any actions which should be taken in respect of:

a) Lily Trading (7 marks)
b) Cekap Berhad (7 marks)
c) Pantas Berhad (6 marks)

(Total: 20 marks)

QUESTION 5

You are the manager responsible for the audit of Logic Berhad, a listed company specialising in the manufacture and installation of sound-proof partitions for domestic and industrial buildings.

You are currently reviewing the draft auditor's report on the company's financial statements for the year ended 31 March 2022. Extracts from the draft auditor's report are shown below:

Independent auditor's report to the shareholders and directors of Logic Berhad

Basis for opinion

We conducted our audit of Logic Berhad (the Company) in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the Company in accordance with the ethical requirements which are relevant to our audit of the financial statements in the jurisdiction in which the Company operates, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

We have audited the financial statements of Logic Berhad (the Company), which comprise the statement of financial position as at 31 March 2022, the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies. In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at 31 March 2022, and of its financial performance and its cash flows for the year then ended in accordance with Malaysian Financial Reporting Standards (MFRS).

Continued ...

Material uncertainty regarding going concern

The Company is financed by a long-term loan from its bankers which is due for redemption in August 2022. At the date of this auditor's report, the Company is in the process of renegotiating the loan but has not yet reached a final agreement with its bankers. It is our view that the loan finance is essential to the continued survival of the Company and that at the time of reporting, therefore, the absence of a finalised agreement represents a material uncertainty regarding going concern. The financial statements have been prepared on a going concern basis but do not make any reference to the loan redemption or the ongoing negotiations with the bank. As the external auditor therefore, we are fulfilling our duty by bringing the matter to the attention of users of the financial statements.

Other information

The Company's principal activity is the manufacture and installation of sound-proof partitions for domestic and industrial buildings. The Company therefore engages in long-term contracts which are incomplete at the reporting date and which are material to its revenue figure. The installation process is complex and significant judgement is applied in assessing the percentage of completeness which is applied to calculate the revenue for the year. The significance of this judgement requires us to disclose the issue as other information which is relevant to the users of the financial statements.

Required:

Critically comment the extract from the draft auditor's report for the year ended 31 March 2022.

Note: You are NOT required to re-draft the extracts from the auditor's report

(Total: 9 marks)

End of Paper